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Circular Letter

TO: ALL PUBLIC AGENCIES

SUBJECT: INFORMATION ON COST IMPACT OF 80 PERCENT PPPA (AB 1009)

The purpose of this letter is to provide information regarding the financial impact of recently enacted legislation. Assembly Bill 1009 (AB 1009) of the 2000 Legislative Session signed by the Governor in September 2000, affects the retirement benefits of all public agency members. This legislation guarantees that the purchasing power of allowances paid to local contracting agency retirees will be maintained at not less than 80 percent of their original purchasing power. Prior to this legislation, the level of purchasing power protection was set at 75 percent, but this was capped at 1.1 percent of employee contributions, system-wide. AB 1009 also provides that each employer will fund the benefits of its own retirees from its own assets, with no limitation on the dollars necessary to provide 80 percent purchasing power.

Under this new legislation, existing retirees currently in receipt of a PPPA payment will get a relatively higher PPPA amount. Existing retirees not yet in receipt of a PPPA payment will start receiving a PPPA payment at an earlier age.

The impact of the 80 percent PPPA will be recognized in the coming annual actuarial valuation as of June 30, 2000. These reports which will contain cost information specific to your plan will be mailed in September and October of 2001. In an effort to provide some guidance on the financial impact of this new legislation, we have examined the impact for a sample of miscellaneous and safety plans representing a cross section of plans.

From a study of these sample plans, we observed that the implementation of AB 1009 increases both the accrued liability and present value of future benefits of each plan by approximately 1 percent to 2 percent. It increases the employer normal cost by roughly 0.1 percent to 0.2 percent of the total payroll for miscellaneous plans and 0.2 percent to 0.5 percent of the total payroll for safety plans. The increase in the total employer rate is comprised of the sum of an amortization of the increase in accrued liability plus the increase in normal cost. For plans with non-zero rates and multiple amortization periods, the increase in the employer rate could go up by as much as 3 percent of total payroll. For well-funded plans with zero rates, there may be no immediate increase in the employer rate. The impact of 80 percent PPPA will be more volatile for smaller plans than for larger plans.

The actual impact for a particular plan will depend on the demographics, plan provisions and funded status of the plan. Plans with retirees who have been retired for an extended period of time will experience higher increases than plans with retirees who have been retired for a shorter period of time. The impact of AB 1009 is usually greater for safety plans than for miscellaneous plans, and greater for plans with the 3 percent @ 50 safety formula than for plans with the 2 percent @ 55 safety formula. Generally, plans which provide an annual regular COLA higher than 2 percent will see a lower impact than plans providing a 2 percent COLA.

The cost impact of changing the method of funding PPPA benefits to have each employer pay the cost of the benefits of its own retirees is negligible across the entire system, since there are very few plans where subsidization from other plans is needed. However, if a plan has a large number of retirees compared to the number of active employees, the cost to that individual plan may be more significant.

If you have any questions regarding the information provided in this letter, please contact your plan actuary.

Kenneth W. Marzion

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